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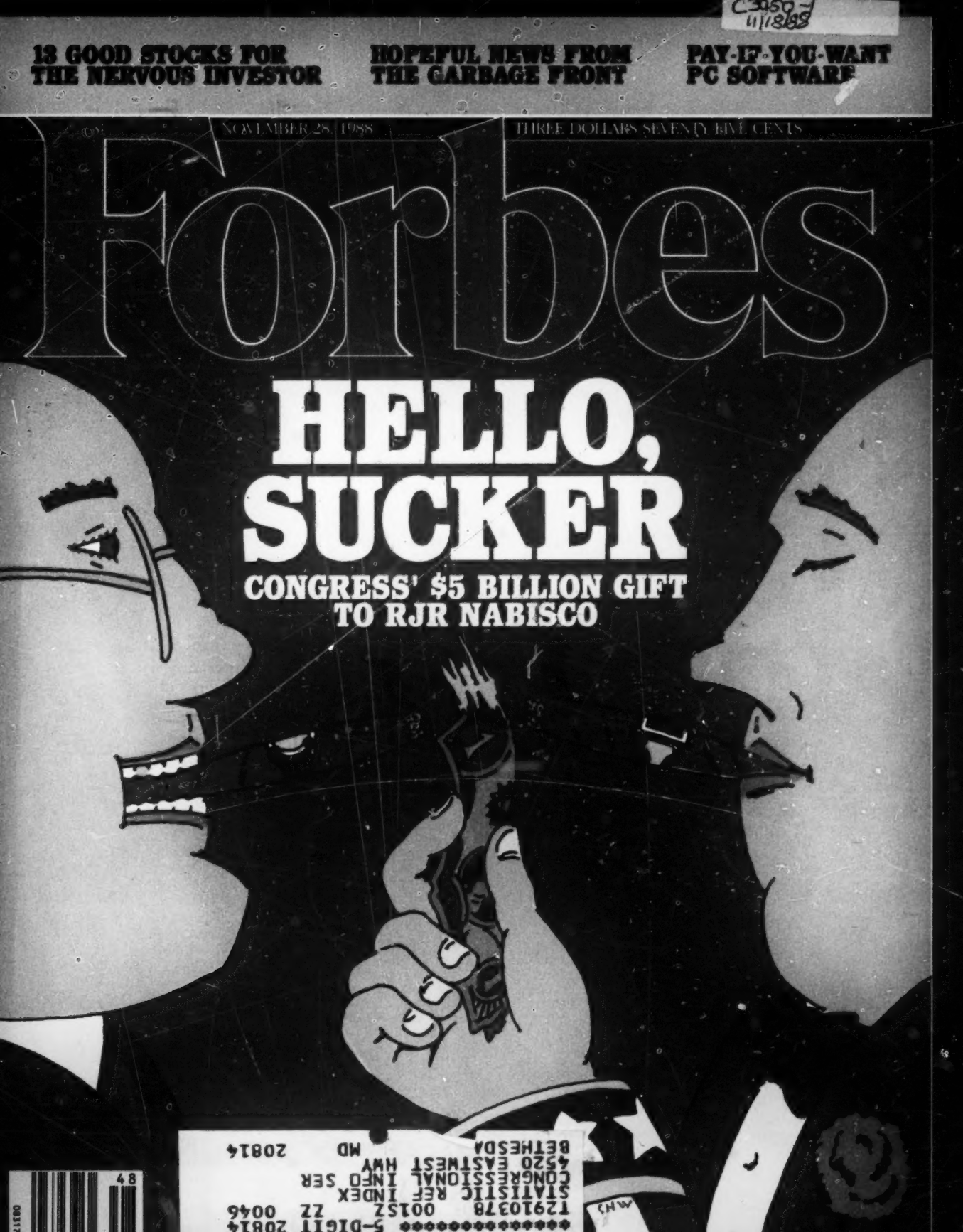

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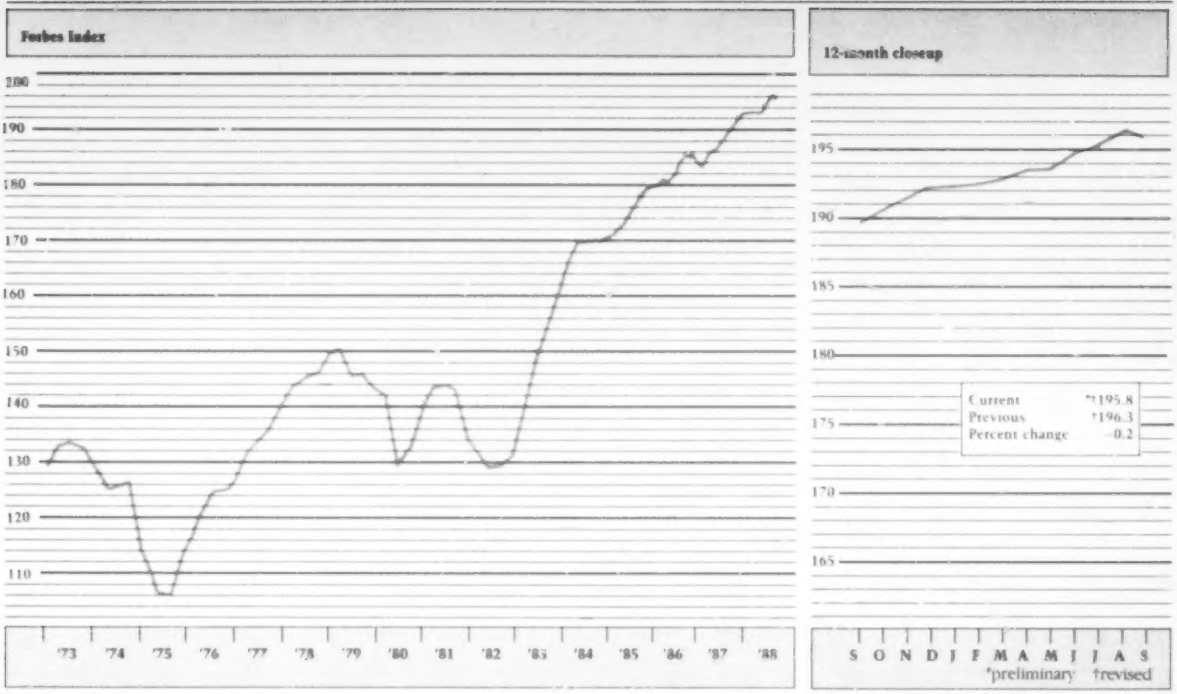
The Forbes Index



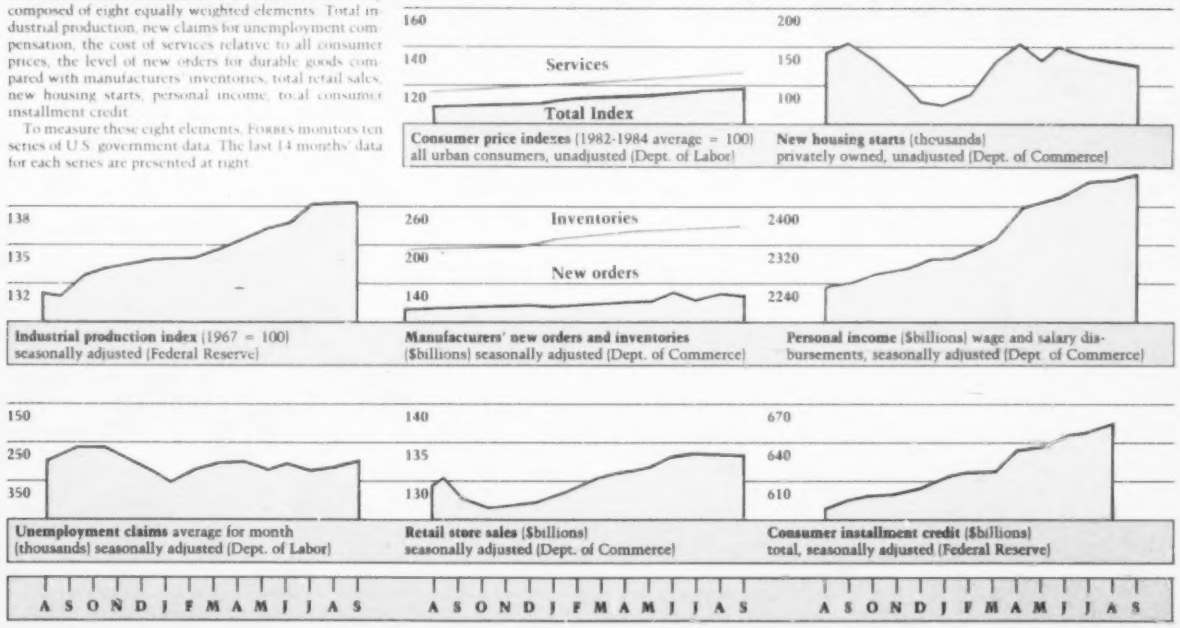
Easing off the gas. The government's index of leading indicators slipped 0.1% in September, its second decline in five months. The latest estimate for gross national product shows that the economy grew at a 2.2% annual rate in the third quarter versus a 3% pace during the second quarter. Manufacturers' new orders fell 3.2% in September, while inventories rose 0.8%.

The sustained economic expansion may be slowing down a bit, but the economy still appears to have considerable momentum. Personal income reached $2.47 trillion in September, an 8.3% gain since the start of the year. In the same stretch the Consumer Price Index rose 3.8%. The October civilian unemployment rate fell to 5.3%, which matches the 14-year low set in June.

The Forbes Index Components

The Forbes Index is a measure of U.S. economic activity composed of eight equally weighted elements. Total industrial production, new claims for unemployment compensation, the cost of services relative to all consumer prices, the level of new orders for durable goods compared with manufacturers' inventories, total retail sales, new housing starts, personal income, total consumer installment credit.

To measure these eight elements, FORBES monitors ten series of U.S. government data. The last 14 months' data for each series are presented at right.


160
140
120
Services
Total Index
Consumer price indexes (1982-1984 average = 100) all urban consumers, unadjusted (Dept. of Labor)
200
150
100
New housing starts (thousands) privately owned, unadjusted (Dept. of Commerce)
138
135
132
Industrial production index (1967 = 100) seasonally adjusted (Federal Reserve)
260
200
140
Inventories
New orders
Manufacturers' new orders and inventories ($billions) seasonally adjusted (Dept. of Commerce)
2400
2320
2240
Personal income ($billions) wage and salary disbursements, seasonally adjusted (Dept. of Commerce)
150
250
350
Unemployment claims average for month (thousands) seasonally adjusted (Dept. of Labor)
140
135
130
Retail store sales ($billions) seasonally adjusted (Dept. of Commerce)
670
640
610
Consumer installment credit ($billions) total, seasonally adjusted (Federal Reserve)
A S O N D J F M A M J J A S
A S O N D J F M A M J J A S
A S O N D J F M A M J J A S

35% of the local market, but is quite unable to start a fare war. Result: Fares in and out of Atlanta are about the highest for any market segment in the U.S.

To a lesser degree, the situation is similar at Delta's smaller hubs like Cincinnati and Salt Lake City, where Delta has local near-monopolies. Industry experts fully expect the action to heat up at Atlanta first. Rumor of the month is that United might buy some of Eastern's gates from cash-starved Frank Lorenzo.

The airline has not always fared well against tough competitors. Some five years ago, for example, when there was a recession and a severe fare war in the northeast New York-to-Florida market, Delta lost money in operating terms. More recently, it has been struggling mightily at Dallas in head-to-head competition with locally dominant American, and only managing to push its market share to around 25% of passenger traffic.

And there are other key areas of the business where Delta has not done well. Its computer reservation system, DataSII, despite an investment of at least $120 million and a software update called DataStar, has, after six years , just 11% of travel agents nationwide signed up. DataSII took in only 6.5% of revenues generated by all such reservation systems, whereas American and United each have over 35% of the market on their systems, which now dominate this increasingly important element of the airline business. Delta faces either further heavy investment in its own reservations computer or, more likely, some observers think, buying a stake in a rival system.

Another chance missed was the relatively small number of top people from Western who stayed with the merged carrier (Delta bought Western last year)—just 4 of 16 officers, despite the offer of higher pay. These newcomers could have injected new life, most importantly, into Delta's marketing operations, a traditional weak spot. Delta, for example is trying to score through its relationship with both Disneyland and Walt Disney World, and has taken a long-term lease on a new $200 million 24-gate hub at Orlando, Fla. It's far from clear, however, whether associating with Mickey Mouse will entice the airline's bread and butter, the full-fare business traveler.

It would be silly, however, to write Delta off. The airline still has plenty of strengths, not the least of which is employee loyalty and morale. Delta's annual compensation for all employees in the first quarter of 1988 averaged $51,400, according to consultants Airline Economics, against $47,100 at Eastern, $44,400 at United, $43,800 at American and $29,700 at Continental. In addition, Delta granted an average 6% pay increase this August. Yet even though it pays the highest wages in the industry, its per-worker productivity is high. Financially, too, the company is a powerhouse: Credits from sale and lease-back deals on planes have helped reduce long-term debt to just $750 million, 33% of equity, against an industry median of over 80%. Cash in hand—$823 million at the end of June—will, however, decline, says Roeck, to cover this fiscal year's planned aircraft buys and investment in its computer reservation system.

What lies ahead is a tough test for the management skills of Ronald Allen, handpicked and trained as his successor by previous chairman David Garrett. How he responds to these problems will tell a lot. Delta has always been distinguished by a relentlessly good-old-boy management style. For example, Allen, 48, still regularly slips across the street to the Dwarf House, his favorite restaurant, for an early country breakfast and small talk with the airline's workers. "Being nice to our workers, paying them well, that's not good ol' boy, it's modern and enlightened," says Allen.

But there is a fine line between enlightenment and permissiveness. A question: Will Allen, as Delta always has, stoutly defend his pilots, right or wrong? Or will he discipline them, in an attempt to defuse things in advance of the National Transportation Safety Board's public inquiry? His inclination is to do things the old way. But this may no longer suffice at a time when this onetime regional airline is spreading its wings over international routes.

Is there an iron core hidden in those good, ol'-style, southern manners? Or will it all turn out to be just fried chicken? All eyes on Ronald Allen. ■

The way things are going, Japan may soon be as much the leader in world banking and money handling as it has become in world manufacturing.

It's a fact of life—creditors call the tune

By Richard L. Stern

THE TABLE ON page 96 was prepared for FORBES by Wall Street analyst Michael Goldstein of Sanford C. Bernstein & Co. It shows—if anyone still needs proof—that Japan is fast becoming as powerful in finance as it has already become in manufacturing. The table compares financial results of Japan's big four brokerage firms with the top 18 in this country. In the U.S. Wall Street is faltering. Margins are wretched in almost every line of business, except in the riskiest parts—mergers and acquisitions and leveraged buyouts.

Japan's biggest brokers rack up a pretax return on equity that is more than five times the Americans'. As it was at first in manufacturing, Japanese overhead in financial services is stunningly low. Japan's big four, with 36,500 employees, paid out $3 billion in compensation and benefits, reaped $21.7 billion in revenues and $10.9 billion in pretax income.

Compare this with the U.S. firms: 183,190 employees, $14.3 billion in compensation and $47.7 billion in revenues, but only $2.3 billion in pretax income. Five times more employees to bring in about 2¼ times more revenues.

One big reason: Japanese brokerage salesmen, except for a small minority, are on straight salary and earn no commissions. Compare that with the average 40% retail commission payout for retail salesmen in the U.S.

But Wall Street is only one side of the Japanese worldwide push into fi-

nancial services. In deposits, the Japanese have the ten largest banks in the world. Citibank, the largest in the U.S., is 28th globally. The increase in the value of the yen is part of the explanation, but the Japanese banks' assets also are growing within Japan.

If this comparison doesn't impress you, nothing will: Annual asset growth of Dai-Ichi Kangyo Bank, the world's largest bank, for example, exceeds the entire asset base of "that bluest of blue-chip banks, J.P. Morgan," notes Tokyo-based J. Brian Waterhouse of the British brokerage James Capel & Co.

Japan's banks, like its brokerages, are not only the largest but also among the lowest-cost producers. The country's legendary high savings rate plus its strict controls on interest paid on deposits has given the Japanese at least a 100-basis-point advantage in spread over the U.S. and most other competitors as well.

Are Japan's competitors alarmed about this? Of course they are. But they are finding there is little they can do. In July, for example, an international body, the Cooke Committee, headed by W.P. Cooke of the Bank of England, appeared to be trying to stop the Japanese by tilting the playing field. The committee recommended, among other things, that by 1993 all banks should have a 4% minimum ratio of shareholder equity to so-called risk-adjusted assets. Forget the technicalities; it was no problem for U.S. or most foreign banks, since most are already over that minimum. But the Japanese banks earlier this year were in the 3.2%-to-3.5% range. It would take billions of dollars and many years for the Japanese to catch up. While amassing more capital, they would be forced to slow their loan growth.

It won't work. The Japanese banks need $37 billion to meet the new standard, and, without even breathing hard, they raised an estimated $14.7 billion through equity offerings in just the July-September quarter of 1988. They will most certainly be in compliance by 1993.

Now the Japanese are contemplating deregulation of their financial markets similar to what is occurring in the U.S. They are considering deregulating brokerage commission rates, a move that set off a wave of brokerage mergers and failures here in 1975 and after. The Japanese also are looking at lowering the barriers between commercial and investment banking and deregulating interest paid on savings. Will that erode some of the cost advantages the Japanese have been enjoying? Don't bet too heavily on that happening. Tokyo is expected to loosen the reins more slowly than we did in this country.

To say all this is not Japan-bashing. It is simply to recognize that Japan is a force to be reckoned with in the world, well beyond the bounds of manufacturing excellence.

If you doubt that Japan intends to spread its influence ever wider in the world, listen to these words from a confidential, narrowly circulated study from Nomura Securities' Nomura Research Institute, *The World Economy and Financial Markets in 1995: Japan's Role and Challenges*. It says, in part, "Just as the U.S. in its best years gave the world GATT and the IMF, which greatly improved the function of the world economy, it is the task of Japan, now the largest creditor nation in the world, to put together a new international framework to meet the demands for an even more integrated and interdependent world community in the 21st century." Nomura is saying: Japan will no longer be a follower; we will become a leader, maybe the leader. ■

Japan's top four versus America's largest brokers

With four times higher expenses, the U.S. brokers produced only 2¼ times the Japanese revenues. No wonder U.S. pretax margins were 1/6th those of the Japanese and return on equity was 1/5th that of the Japanese.

Category	Nomura Worldwide	Daiwa Securities	Nikko[1] Securities	Yamaichi Securities	Total	The 18 largest U.S. brokers
Brokerage commissions	$4,629	$2,396	$2,202	$2,554	$11,780	$8,750
Underwriting and distribution	1,400	835	774	940	3,949	4,750
Net gain on trading	1,024	306	474	5	1,809	5,750
Interest and dividends	1,401	1,398	67	694	3,560	23,150
Other	62	183	180	211	636	5,250
Total revenues	8,516	5,118	3,697	4,404	21,735	47,650
Compensation and benefits	1,088	623	564	719	2,995	14,250
Interest expense	781	1,093	194	403	2,471	21,175
All other expenses	2,016	1,084	1,063	1,113	5,276	9,925
Total expenses	3,885	2,800	1,821	2,236	10,742	45,350
Income before taxes	4,631	2,318	1,876	2,168	10,993	2,300
Nonoperating income & other	0	(39)	31	15	6	NA
Taxes	2,503	1,264	1,055	1,168	5,990	NA
Net income	2,128	1,016	851	1,016	5,010	NA
Pretax margin[2]	60%	58%	54%	54%	56%	9%
Average shareholders' equity	6,950	3,413	3,287	3,197	16,845	19,000
Pretax return on equity	67%	67%	58%	68%	65%	12%

All figures in millions of dollars; prices have been rounded. [1]Financial statement excludes unconsolidated subsidiaries. [2]Revenues include net interest. NA: Not available.

Source: Sanford C. Bernstein & Co.

And we mean quiet

Nestled in the British Virgin Islands, a chip shot off Tortola, lies the tiny Guana Island Club, which even picky Andrew Harper raved about in his *Hideaway Report* ("This just may be the most private and unspoiled resort island in the West Indies"). Only 30 guests can be accommodated. Dining is family-style (no restaurant means there are no interloping yachtsies).

Six deserted beaches await you. Cozy guest cottages make up in quiet what they lack in elegance. Rates: $385 double per day, including meals and tennis, Dec. 16 to Mar. 31.

Sotheby's Art Market Trends

Index sectors	Oct 1988	One month ago	One year ago	Two years ago	Five years ago	One month % change	One year % change	Two years % change	Five years % change	Five years average annual % change
Old Master paintings	403	403	349	303	217	nil	+15.5	+33.0	+85.7	+13.2
19th-century European paintings	361	361	323	250	197	nil	+11.8	+44.4	+83.2	+12.9
Impressionist & Post-Impressionist art	1,091	1,091	661	432	298	nil	+65.1	+152.5	+266.1	+29.6
Modern paintings (1900-1950)	1,090	1,090	666	429	275	nil	+63.7	+154.1	+296.4	+31.7
Contemporary art (1945 onward)	728	728	597	542	383	nil	+21.9	+34.3	+90.1	+13.7
American paintings (1800-pre-WWII)	958	958	789	687	501	nil	+21.4	+39.4	+91.2	+13.8
Continental ceramics	467	407	320	290	272	+14.7	+45.9	+61.0	+71.7	+11.4
Chinese ceramics	684	684	550	486	445	nil	+24.4	+40.7	+53.7	+ 9.0
English silver	388	388	349	338	219	nil	+11.2	+14.8	+77.2	+12.1
Continental silver	260	260	201	192	156	nil	+29.4	+35.4	+66.7	+10.8
American furniture	469	469	459	380	239	nil	+ 3.8	+23.4	+96.2	+14.4
French & Continental furniture	359	355	319	285	257	+1.1	+12.5	+26.0	+39.7	+ 6.9
English furniture	784	784	594	447	309	nil	+32.0	+75.4	+153.7	+20.5
Aggregate index*	661	660	477	369	275	+0.2	+38.6	+79.1	+140.4	+19.2

Basis: 1975 = 100 ($). ©Sotheby's 1988

*Contemporary art was added to the Art Index in September 1987. The aggregate index excludes this category prior to that date.

Sotheby's Art Market Trends reflect subjective analyses and opinions of Sotheby's art experts, based on auction sales and other information deemed relevant. Nothing in Sotheby's Art Market Trends is intended as investment advice or as a prediction or guarantee of future performance or otherwise.

Monthly highlights

The New York jewelry auctions in October were strong overall, totaling more than $60 million. Eleven gems were sold for over $1 million each, including a 15.97-carat Burmese ruby that fetched $3.6 million, a record for any colored stone. However, two major gems with high preauction estimates failed to sell: a 48.02-carat Burmese ruby and a 407.48-carat diamond. Given the difficulty of estimating stones of this kind, it's impossible to draw any broad conclusions about their failure to sell.

The latest sales in New York of French furniture, which traditionally draw an international mix of clients, were reinforced by the growing interest of American private buyers, notably younger collectors. Overall, the sales were a success. Top quality and rare furniture and decorative items brought premium prices. Furniture that did not rank among the best fared less well and often sold below the low estimate. Results confirmed the recent strength of the Louis XVI period but also indicated a slight contraction in the market for more elaborate Louis XIV pieces.

Sotheby's

Louis XVI Ormolu-mounted consoles

The major sales that took place in New York toward the very end of the month of Old Master and 19th-century European paintings, as well as of English furniture and silver, gave further evidence of the overall strength of the art market. A sale of 19th-century European paintings realized $15.3 million, a worldwide auction record.

Following the British Rail Pension Fund's auction in London in September of books and manuscripts, the fund's Continental porcelain collection produced good results. Nine of the top ten lots of the sale, which also included property from other sources, came from this collection, and each achieved between three and six times the original purchase prices paid in the late Seventies.

Considering a detour to Washington? The money's lousy and the hours are long. But as a launching pad back into private industry, you just can't beat the experience.

Costly but priceless

By Dyan Machan

With a new Administration set to take over the White House in two months' time, some 5,000 presidential appointments are once again up for grabs. If the phone rings in your house with an offer, should you accept it? One source of guidance might be a tome nicknamed the "Plum Book," a quadrennial listing of all 5,000 government jobs, their current holders and salaries. Now, the Washington-based Center for Excellence in Government, an organization of 400 former high-level appointees, has published a knockoff called *The Prune Book*. It lists the best of what's found in the larger listing—the 100 most important and powerful presidential appointments in the executive branch.

The Prune Book lists not only titles and responsibilities but current and past holders of the offices over 19 years. Additionally, each job entry includes lengthy and detailed information on what sorts of qualities and skills are demanded of the successful appointee, as well as a rundown of dos, don'ts and get-ahead tips.

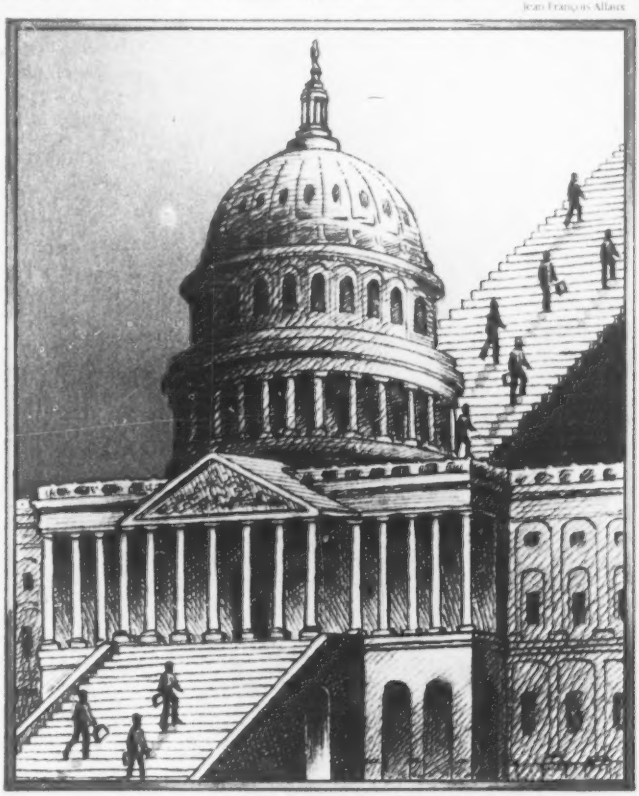
Reading *The Prune Book*, one is struck by an obvious theme that runs throughout nearly all the entries. Though responsibilities and political clout vary widely from job to job, and though salary levels are often appallingly low for the duties involved, landing a *Prune Book* job can really prove to be a plum of a stepping-stone back into the private sector later on.

If Norman Augustine, 53, hadn't gotten that call from the Johnson Administration back in 1965, he'd probably still be at Douglas Aircraft instead of chairman of Martin Marietta. But the chief engineer at Douglas packed up his wife and two babies and headed for Washington to run the research and engineering sections in the Defense Department. His wife's reaction to leaving their home in Santa Monica, Calif. for a boxy rental in McLean, Va.? "She cried."

Augustine left for a senior post at LTV in 1970, but returned to Washington in 1973 as assistant secretary of the Army for R&D under Richard Nixon. The result was an instant 50% cut in his $60,000-a-year pay at LTV, and to make ends meet his wife had to get a job. But the resulting experience of helping manage the largest branch of the armed forces made him a natural candidate to join Martin Marietta, a major defense contractor, which he did in 1977. Says Augustine of his time in Washington, "It was the hardest I've ever worked in my life, including now. But if I were 30 years old and were given the same opportunity, I would do it again. Absolutely."

Frank Herringer went to Washington in 1972, at the age of 28. He had just finished six years as a management consultant with Cresap, McCormick & Paget, yet jumped at the chance to take a $10,000 pay cut to become a $22,000-a-year White House personnel staffer for Richard Nixon. Two years later he was named administrator of the Urban Mass Transportation Administration. Back in the private sector in 1979, he joined Transamerica Corp. as an assistant to the chairman. Seven years later he was president, and today has a base salary of $800,000. Says Herringer, now 45, of his Washington experience, "I don't think the credential itself has been that important, but the experience certainly was."

Government was truly a stepping-stone for Paul O'Neill, 52, who went to Washington in 1961 as a 25-year-old Veterans' Administration intern, earning the princely sum of $6,435 a year. By 1974 O'Neill was deputy director for the Office of Management & Budget, yet was well aware that with college-age kids he needed a heftier income than his $44,000-a-year OMB salary provided.



Jean-François Allaux

But 13 years in Washington had brought him so many contacts that he scarcely had to whisper his career-switch plans to friends for unsolicited job offers to begin pouring in.

O'Neill chose an offer to become vice president of planning for International Paper at $115,000 a year. Seven years later, in 1985, he was named president of the company, and last year was tapped by Alcoa to become chairman and chief executive officer at a base salary of $575,000. O'Neill says of his career, "What I've been doing for most of my life is following my nose. The only uniformity in what I've been doing is looking for an opportunity and making a contribution. It's paid off very nicely."

For how others have fared after Washington duty, see table below.

Prune Book biggies

How do you gauge the effect of Washington service on one's career? Take a look at some of the government servants who passed through the Office of Management & Budget in recent years.

Edwin L. Harper, 47
Prior job: V.P., Emerson Electric. **Pay:** $180,000.
OMB job: Deputy director (1981-82). **Pay:** $60,000.
Present job: Chief financial officer, Campbell Soup Co. **Pay:** $300,000-plus.
Quote: "The family's structure is completely focused on the appointee's role. It can be disorienting."

Edward Jayne II, 44
Prior job: Air Force officer. **Pay:** $40,000.
OMB job: Associate director for National Security & International Affairs (1977-81). **Pay:** $52,000.
Present job: V.P., strategic program development, McDonnell Douglas. **Pay:** $132,000-plus.*
Quote: "When ready to leave, I had two dozen offers or strong job leads."

Brian Smith

Daniel Kearney, 49
Prior job: Executive director of Illinois Housing Development Authority. **Pay:** $32,000.
OMB job: Associate director for Economics & Government (1976-77). **Pay:** $36,000.
Present job: Principal, Aldrich, Eastman & Waltch. **Pay:** $400,000-plus
Quote: "When you are passing out dollar bills, a lot of people think you are a great guy."

Frederick Khedouri, 38
Prior job: Legislative director for Representative David Stockman.
OMB job: Associate director for natural resources, energy and science (1981-85). **Pay:** $72,000.
Present job: Associate director of Bear, Stearns. **Pay:** $300,000-plus.**
Quote: "I would leave before my son got up and get home after he went to bed."

Maurice Mann, 59
Prior job: Chief economist for Federal Reserve Bank in Cleveland. **Pay:** $9,000.
OMB job: Associate director for natural resources, energy and science (1969-70). **Pay:** $38,000.
Present job: Chairman of Pacific Stock Exchange. **Pay:** $500,000-plus.
Quote: "There's nothing more exciting than eating breakfast in the White House mess."

Paul O'Neill, 52
Prior job: OMB staff. **Pay:** $36,000.
OMB job: Deputy director (1974-77). **Pay:** $44,000.
Present job: Chairman and chief executive officer, Aluminum Company of America. **Pay:** $575,000 base salary.
Quote: "I worked every single day except for Christmas. It tires your family out."

Franklin Raines, 39
Prior job: Assistant director, domestic policy staff for Carter Administration. **Pay:** $33,000.
OMB job: Associate director for economics and government (1978-79). **Pay:** $50,000.
Present job: General partner, Lazard Frères. **Pay:** $250,000-plus.
Quote: "What do you do with somebody who was running a quarter of the federal budget but who had only six months' experience as a lawyer?"

John Sawhill, 52
Prior job: Executive vice president, Commercial Credit. **Pay:** $110,000.
OMB job: Associate director for natural resources, energy and science (1973-74). **Pay:** $37,000.
Present job: Senior partner and director at McKinsey. **Pay:** about $600,000.
Quote: "Someone once said the experience is costly, but also priceless."

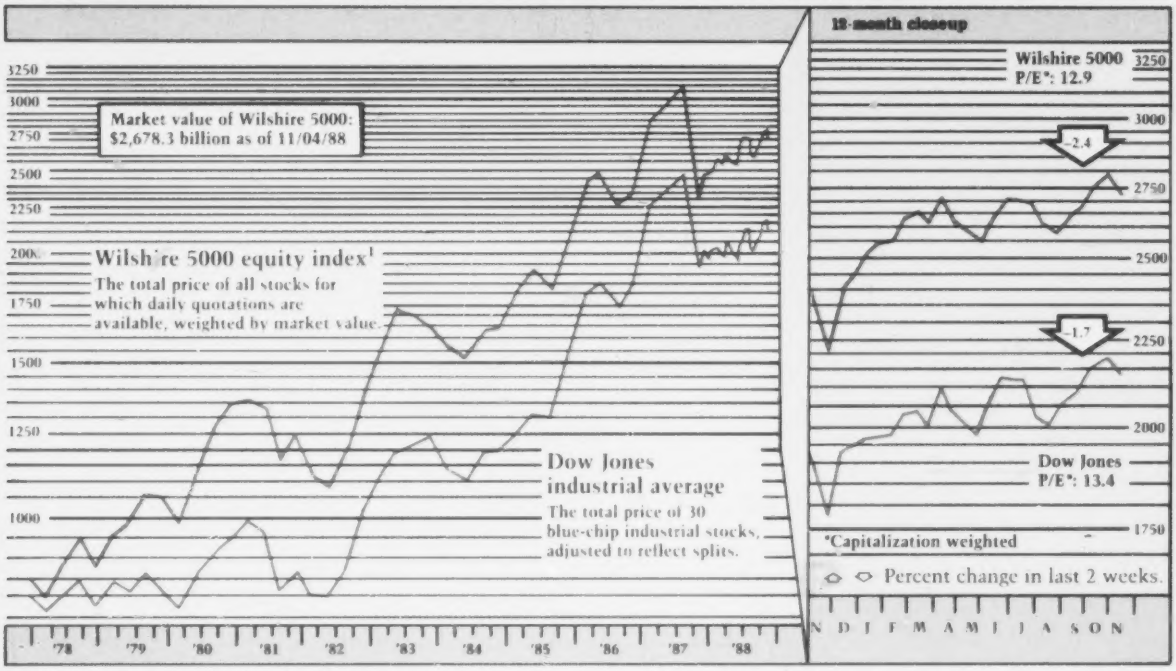
John White, 51
Prior job: Senior V.P., Rand Corp. **Pay:** $65,000.
OMB job: Deputy director (1978-81). **Pay:** $47,000.
Present job: V.P. at Kodak. **Pay:** $117,000-plus.*
Quote: "We gave up the ocean view in Malibu for McLean, Va."

Frank Zarb, 53
Prior job: An investment banker for Shearson. **Pay:** $180,000.
OMB job: Associate director for natural resources, energy and science (1974-75). **Pay:** $60,000.
Present job: Chairman and chief executive officer of Smith Barney. **Pay:** $1 million.
Quote: "A turkey in government is a turkey in business."

*Salary estimate supplied by a Mercer Meidinger Hansen survey
**Salary estimated from a survey by the Whitney Group

The Forbes/Wilshire 5000 Review

Edited by Steve Kichen



Declining prices tend to bring out the pessimists. *Investors Intelligence*, a New Rochelle, N.Y. newsletter, has tracked the ratio of bullish to bearish investment advisers for over 25 years. Editor Michael Burke notes that the ratio briefly climbed above 1 this Oct. 19—i.e., there were more bulls than bears. That was a good time to sell into strength. Two days later the Dow hit a postcrash high.

Now, only a few weeks later, Burke's indicator shows a ratio of 0.78 (35 bulls to 45 bears). But that isn't a bad sign for the market. The last time there was a considerable amount of bullishness was August 1987, just when the market peaked. That's why sentiment indicators such as Burke's are used by many as contrarian indicators. Burke insists that no correction is due until the ratio exceeds 1. And so Burke now expects stock prices to rise as available cash is moved into the market.

Over the last two weeks the Dow industrials dropped 1.7%, while the Wilshire index was off 2.4%.

Closeup On the Equity Markets

Performance of six leading indexes

Percent change	Wilshire 5000	Forbes 500[2]	Dow Jones industrials	NYSE Composite	Amex Market Value Index	NASDAQ Composite
in last 4 weeks	–1.0	–0.6	–0.2	–0.7	–2.1	–1.2
in last 52 weeks	11.9	10.5	9.5	11.2	16.6	16.7

Stock performance based on six key investor yardsticks

Percent change	Company size		Volatility[3]		P/E multiple		Dividend yield		Growth profile[4]		Share price	
	large	small	high	low	over 21	under 8	over 4.5%	none	high	low	over $34	under $4
in last 4 weeks	–1.6	–0.5	–1.1	1.2	–1.9	0.6	–0.9	2.4	–1.4	0.1	–0.6	–2.7
in last 52 weeks	15.6	51.5	59.3	24.8	27.3	30.0	17.8	69.6	56.9	24.7	20.8	42.4

[1]Wilshire index reflects price performance. It differs slightly from market value of outstanding stocks because of retirements of equity since index was created. [2]Based on sales. [3]A stock's sensitivity to overall market movement. High-volatility issues have wide price fluctuations, low-volatility issues are more stable. [4]A quantitative evaluation of a stock's growth image, determined by Wilshire Associates.

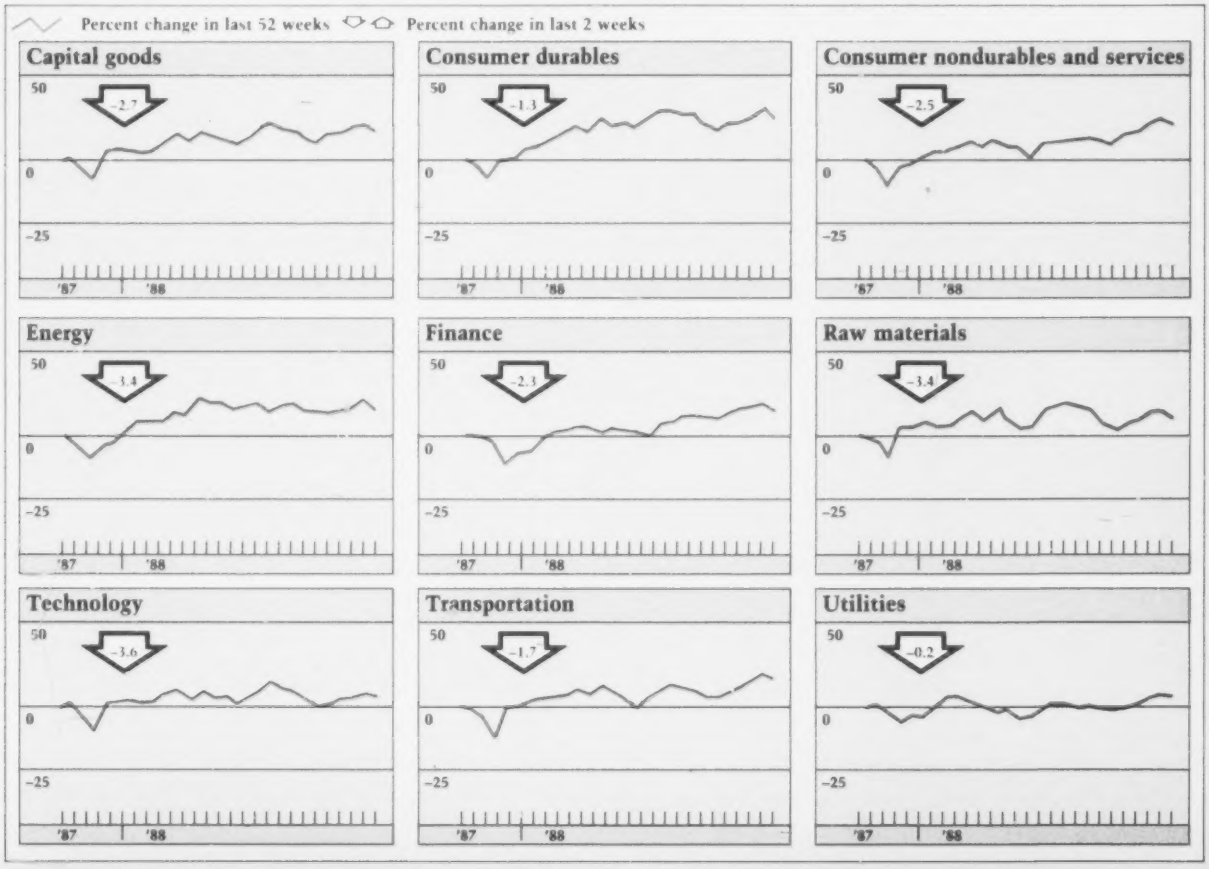
Note: All data for periods ending 11/04/88. Prepared by Wilshire Associates, Santa Monica, Calif.

Steven Kichen

Where the Action Is

Utility stocks, of the nine Wilshire sectors, show the smallest two-week loss and the only gain over the last four weeks. Gary F. Hovis, director of utility research at New York-based Argus Research, explains the recent popularity of utilities: "If we ever got in a real whiz bang of a recession and a lot of this leveraged buyout debt defaulted, then the assets behind a utility are a safety factor." Hovis thinks investors are also attracted by the potential returns of utilities: "With [some] sound utility stocks today the yield is around 8% to 8.5%, and you could probably get 2 or 3 stock points in a year" of price appreciation. That would generate a total return of 14% to 15%.

Technology was the weakest-performing group over the last two weeks. Cray Research fell almost 20%.



What the Analysts Think

Analysts responded to healthy fall auto sales by raising 1988 earnings estimates for several auto manufacturers. Forecasts for Honda, General Motors and Ford were raised in the last two weeks from 14 cents to 22 cents. Chrysler's 1988 estimate was cut by a dime. The consumer durables sector shows the best improvement in earnings estimates.

Forecasting the Forbes Sales 500

Performance period	Average earnings per share	P/E
latest 12 months	$3.25	12.1
1988 estimates	3.58	11.0
1989 estimates	3.96	9.9

Rank based on change in estimate	Sector	Estimated 1988 EPS	Estimated 1988 P/E	% change in 1988 estimate in 2 weeks	% change in 1988 estimate in 4 weeks
1	Consumer durables	$4.83	10.8	0.66%	0.95%
2	Transportation	2.27	12.2	0.37	0.62
3	Raw materials	3.19	9.5	0.17	0.16
4	Capital goods	2.61	14.0	0.05	-0.41
5	Consumer nondurables	2.51	14.3	-0.07	-0.35
6	Utilities	2.38	10.5	-0.10	-0.22
7	Energy	3.23	12.0	-0.11	-0.25
8	Finance	3.36	8.8	-0.33	-1.00
9	Technology	2.97	11.6	-0.54	-1.36

Earnings projections are capitalization-weighted consensus estimates from over 3,000 security analysts. Data are compiled and updated continually by the Institutional Brokers Estimate System (IBES), a service of Lynch, Jones & Ryan, a New York-based brokerage firm.

Note: All data for periods ending 11/04/88. Prepared by Wilshire Associates, Santa Monica, Calif., IBES, a service of Lynch, Jones & Ryan, New York.

The Forbes/TUCS Institutional Portfolio Report

Edited by Steve Kichen

In our quarterly review of institutional portfolios, IBM sticks out as an unfavorite. It is the most underrepresented stock (relative to its size) and gets more so all the time. The table on the facing page, "Where the institutions are," shows that IBM makes up 4.3% of the Wilshire 5000 but only 1.7% of the typical institutional stock portfolio. In the table below at right, "Position changes," IBM tops the selloffs. Institutions liquidated 6.3% of their shares in the third quarter, contributing to IBM's weak performance.

In the 12 months ended Sept. 30, beginning just before the crash, the market obviously did not fare well. But some styles of stock picking fared better than others. So-called value investors, who look for low price/earnings and low price/book value ratios, lost a median 7.1% over the past four quarters. Growth-stock managers, on the other hand, were off a median 13.2% *(see table below at left)*.

While the market was falling, pension funds were cashing out. The table at right, "Segment performance and cash flows," shows that institutions reduced their equity by 2.3%. (This figure is adjusted to back out any changes in the value of the underlying securities.) Were they shifting into bonds? No. They cut their bond portfolios by 8%. Yet, since bonds provided a healthy 12.3% positive return over the period, the funds' final bond position was up slightly.

Pension accounts experienced a net outflow of 5.2% of assets over the past year. How come? With interest rates high, many corporate pension pools became overfunded; as a result, many managements drew down the overfunding for corporate purposes or for helping to finance buyouts. All these data come from Santa Monica-based Wilshire Associates. Wilshire's Trust Universe Comparison Service monitors over $360 billion in 4,500 pension fund accounts.

While equity and fixed income were liquidated, institutional cash holdings were up by 3.6% for the quarter ended Sept. 30, to 10.8% of the portfolio. To a contrarian, then, both stocks and bonds may be good buys. Bennett Shaver, executive director of the Maryland state retirement fund, seems to think they are. Shaver gained recognition for his timing in moving almost 30% of his portfolio's assets out of stocks right before last October's collapse. Since then, however, he has cut his cash to 6%. "I'm not surprised to see a number of people increasing their exposure to cash, [which] dampens the volatility of the whole portfolio," he says. He just thinks their timing is wrong.

How different managers performed

Manager style	Total return[3] recent quarter	12 months	24 months[4]
Diversified	0.4%	–9.3%	12.1%
Growth	–1.2	–13.2	11.1
Growth—emerging	–1.7	–9.7	10.7
Market timer	0.6	–9.6	11.5
Sector rotator	–0.5	–10.5	9.5
Value	1.3	–7.1	11.7

Where the institutions put their money

Segment	—Portfolio weighting— most recent quarter	previous quarter
Equity	60.0%	60.1%
Fixed income	28.6	28.9
Cash and equivalents	10.8	10.4
Convertibles	0.1	0.1
Other[1]	0.5	0.5

Equity portfolio characteristics

	Institutional portfolios	Wilshire 5000
Price/earnings ratio	14.7	13.2
Dividend yield	3.4%	3.3%
Beta[2]	1.05	1.06
Price/sales ratio	1.30	1.36
Price/book ratio	2.81	2.35

Segment performance and cash flows

Segment	—Most recent quarter— median total return	shift in institutional holdings	—Latest 12 months— median total return	shift in institutional holdings
Equity	–0.1%	–0.7%	–11.2%	–2.3%
Fixed income	1.8	–1.6	12.3	–8.0
Cash equiv	2.0	3.6	7.5	0.3
Convertibles	–0.1	–0.3	–4.5	–1.9
Other[1]	0.8	–0.1	7.3	–3.8
Total	0.5	–1.2	–1.1	–5.2

Position changes: These securities had the greatest relative change in holdings over the last quarter

Security	Increase in holdings	Total quarter return	Security	Decrease in holdings	Total quarter return
Wal-Mart	3.1%	5.4%	IBM	–6.3%	–8.6%
Amoco	2.3	2.5	Exxon	–6.2	–0.2
Bell Atlantic	2.1	1.6	General Motors	–3.8	–4.9
Am Info Tech	1.7	4.8	General Electric	–3.2	–0.3
Quaker Oats	1.6	22.3	Ford Motor	–2.8	–2.9
Kroger	1.5	60.1	Mobil	–2.6	–0.7
Coca-Cola	1.5	13.0	Caterpillar	–2.5	–14.9
American Intl Gp	1.5	13.7	Hewlett-Packard	–2.5	–10.4
Apple Computer	1.4	–6.3	ITT	–2.3	–3.5
Waste Mgmt	1.4	18.0	Schlumberger	–2.3	1.7

[1]Real estate, foreign investments, venture capital, guaranteed insurance contracts. [2]A measure of risk. A stock with a beta of 1.00 tends to move up or down at the same rate as the S&P 500. [3]Includes all forms of investments. [4]Figures for 24 months are annualized.

Note: Data for quarter ending 9/30/88. Prepared by the Trust Universe Comparison Service (TUCS®), a service of Wilshire Associates, Santa Monica, Calif.

Where the institutions are—and aren't

Most overweighted relative to Wilshire 5000			Most underweighted relative to Wilshire 5000		
	% of			% of	
Security	institutional universe	Wilshire 5000	Security	institutional universe	Wilshire 5000
Apple Computer	0.7%	0.2%	IBM	1.7%	4.3%
Philip Morris	1.3	1.0	Exxon	0.6	3.0
Waste Mgmt	0.6	0.3	General Electric	1.2	2.3
Compaq Computer	0.3	0.0*	Royal Dutch Petroleum	0.4	1.5
Computer Associates	0.3	0.0*	British Petroleum	0.2	1.2
Warner Communications	0.4	0.2	AT&T	0.6	1.6
MCI Communications	0.3	0.1	El du Pont de Nemours	0.5	1.2
Alcoa	0.4	0.2	Chevron	0.4	0.9
K mart	0.5	0.3	Mobil	0.5	1.0
Wal-Mart	1.0	0.8	BellSouth	0.6	1.1

Honda is now one of the big three. For the first time, pension fund managers are holding more stock in Honda than in Chrysler. The Japanese automaker had a total return of 27.1% for the quarter while the three domestic firms showed small losses. Meanwhile, the institutions sharply reduced their energy holdings, from 9.3% of the TUCS universe in June to only 7.3% in September. Exxon, Mobil and Schlumberger posted the biggest decreases in holdings of the energy group. Of the ten stocks most underweighted in pension portfolios relative to the Wilshire index, five are energy companies. This might be a good time for patient contrarian investors to look at the oil industry.

Sector activity and top holdings

% of institutional portfolio: ■ most recent quarter ■ previous quarter

Capital goods	5.8% 5.4%	Consumer durables	3.9% 4.8%	Consumer nondurables	30.4% 28.1%
	total return		total return		total return
General Electric	–0.3%	General Motors	–4.9%	Philip Morris	16.7%
Emerson Electric	–6.5	Ford Motor	–2.9	Merck	3.3
Westinghouse Electric	–5.3	Honda Motor	27.1	Wal-Mart	5.4
Caterpillar	–14.9	Chrysler	–0.5	Coca-Cola	13.0
Deere & Co	–3.1	Goodyear Tire & Rubber	–9.5	Sears Roebuck	4.9
Energy	**7.3% 9.3%**	**Finance**	**12.6% 12.3%**	**Raw materials**	**14.9% 14.1%**
	total return		**total return**		**total return**
Amoco	2.5%	American Express	2.5%	Waste Management	18.0%
Exxon	–0.2	American Intl Group	13.7	Dow Chemical	–3.5
Atlantic Richfield	–2.7	Citicorp	6.7	El du Pont de Nemours	–11.0
Mobil	–0.7	JP Morgan	–2.3	Alcoa	–0.3
Royal Dutch Petroleum	–1.7	Cigna	15.8	Monsanto	–10.4
Technology	**16.6% 16.5%**	**Transportation**	**3.7% 4.4%**	**Utilities**	**4.8% 4.8%**
	total return		**total return**		**total return**
IBM	–8.6%	Union Pacific	–7.0%	AT&T	–1.7%
Digital Equipment	–18.3	Federal Express	7.2	BellSouth	–2.1
Apple Computer	–6.3	Norfolk Southern	2.0	Nynex	0.4
Boeing	9.9	CSX	14.9	Bell Atlantic	1.6
Hewlett-Packard	–10.4	Ryder System	–16.3	GTE	13.4

*Exact figure is less than 0.05%.